

Controls Over Contracts and Agreements are Crucial

FDIC and the Resolution Trust Corporation (RTC) have relied heavily on goods and services acquired from the private sector to accomplish the mission of managing and selling assets of failed banking and savings institutions. Over the past 7 years, FDIC and RTC have spent several billions of dollars in contractor fees to assist the corporations in fulfilling the myriad of time-critical assignments mandated by legislation and the banking and thrift industry crises. Notwithstanding RTC's sunset, FDIC continues to rely on the private sector to accomplish its mission. Projections of 1997 contract awards and purchases total 14,600 contracts valued at \$400 million. Although this a significant decrease from 1992 when FDIC/RTC spent \$3 billion on contracts, continuing audit coverage is required.

FDIC is also responsible for a number of financial assistance agreements. Generally, assistance agreements have been used as an inducement for investors to acquire failed institutions. Investors acquiring troubled banks and savings institutions receive financial support through such an agreement. Further, an assistance agreement provides protection to the acquiring association or institution against losses incurred for the management and disposition of assets acquired from failed thrifts. FDIC inherited responsibility for administering these agreements from the Federal Savings and Loan Insurance Corporation (FSLIC) with the passage of the Financial Institutions Reform, Recovery and Enforcement Act. The Corporation is currently resolving ongoing issues relating to approximately 70 assistance agreements. Millions of dollars may be involved with a single agreement.

The magnitude of contracts and agreements transitioned from RTC and FSLIC, and additional contracts awarded by FDIC present enormous challenges to the Corporation. Specifically, the goods and services needed by the Corporation must be solicited, competitive bids evaluated, and contracts awarded to the deserving bidder. Throughout that effort, the Corporation also strives to achieve its overall goal of encouraging minority and women owned business participation. The challenges continue after the contracts are awarded. During the performance of the contract, the contracts must be monitored/overseen, invoices for goods and services have to be paid, and disagreements with contractors have to be resolved. As for the assistance agreements, FDIC must be sure that claims for financial assistance are supported and all payments made and credits due are correct.

OIG PROVIDES COVERAGE OF CONTRACTING RISKS AND ISSUES

Although necessary to complete its mission, the extensive use of and reliance on contractors increase the Corporation's exposure to fraud, waste, and abuse. In conducting its work, the OIG seeks to lessen the Corporation's exposure and add value to corporate operations. The OIG continues to devote a significant portion of its resources in the area of contract and agreement oversight. During the past reporting period, the OIG issued 58 products related to contracting issues. These reports questioned \$6.5 million. Various offices within the OIG-- Office of Audits, Office of Congressional Relations and Evaluations, Office of Quality

Assurance and Oversight, and Office of Investigations--have contributed to the overall effort of auditing and reviewing contractors and assisting management in minimizing risks in contracting and assistance agreement activities, as illustrated in the following examples.

CONTRACT AWARD EVALUATED

OIG's Office of Congressional Relations and Evaluations completed an evaluation of the solicitation and award process for the FDIC Southwest Service Center's (SWSC) contract with CB Commercial Real Estate Group and RPC-Mitchell/Titus, Inc.'s subcontract with Terra Commercial, Inc., for real estate brokerage services. We conducted this evaluation in response to inquiries from two Congressmen and a Senator. The congressional inquiries related to concerns expressed to them by bidders who did not get the award in spite of submitting lower cost proposals than the winning bidder.

The results of our review showed that SWSC and RPC-Mitchell/Titus, Inc., generally complied with applicable FDIC or RTC contracting policies and procedures in the award of the subject contract and subcontract. SWSC's contract award was based on the winning offeror's superior technical expertise and sales experiences. SWSC concluded that the winning offeror represented the best value for FDIC, which is one of the basic policy objectives of FDIC's acquisition process. With regard to RPC-Mitchell/Titus's award, the winning offeror received a higher overall rating than other bidders because RPC-Mitchell/Titus weighted technical scores more heavily than cost scores, and appropriately added minority- and women-owned business bonus points to the winning offeror's score.

We did, however, report several observations related to SWSC's evaluation of proposals that we believed warranted management's attention. Our observations specifically involved (1) the basis for certain weaknesses attributed to two offerors by the Technical Evaluation Panel (TEP), (2) SWSC's failure to clearly communicate to offerors that experiences in selling golf courses would be a significant factor in evaluating proposals, and (3) independence of the TEP Chairperson. Management responded that our report raised legitimate concerns. Management also indicated that a training course is currently being developed for conducting TEPs that it believes will improve the proposal evaluation process for both program and contracting operations.

OIG QUESTIONS CONTRACTOR BILLINGS

During this semiannual reporting period, the Office of Audits completed an audit of Arthur Andersen & Co.'s billings to RTC under a due diligence contract. The audit resulted in the OIG questioning approximately \$2.1 million of the \$10.9 million Arthur Andersen billed to RTC for services rendered. The OIG questioned this amount because Arthur Andersen billed (1) employees' time that was different from time records, (2) unallowable and undocumented professional fees, (3) unsupported costs, (4) unallowable independent contractor mark-ups, (5) incorrect occupational categories, and (6) unallowable and unsupported travel and other costs. Of the approximately \$2.1 million the OIG questioned, the Corporation disallowed \$1,039,370 and recovered \$400,000 through a settlement agreement with Arthur Andersen.

The Office of Audits also completed audits of two contracts awarded to Peterson Consulting

Limited Partnerships. Peterson's services included settlement, accounting, and asset operations activities. The OIG questioned \$536,838 of the \$2.1 million billed by Peterson because the billings did not conform with the contract or represented charges that were not allowable under the contract terms. Of the amount questioned, FDIC management did not agree to disallow \$301,772 related to subcontractor markups. The OIG continues to believe that the questioned costs have merit.

The OIG's Office of Congressional Relations and Evaluations conducted a review of Shared Technologies Fairchild (STF) billings to FDIC, in response to a concern from the Associate Director, Acquisition Services Branch, that STF had overbilled or erroneously billed FDIC for telephone services and equipment. The review found that STF overcharged FDIC for long-distance calls in excess of the flat \$0.15 per minute as required by the contract and for monthly charges for local telephone company trunk lines that FDIC actually did not use or require for its level of use.

The OIG also determined that STF and FDIC had fundamentally different interpretations on several key issues under the contract and, therefore, disagreed on the extent of overcharges. Examples of the disagreements due to different contract interpretations include what geographic areas are considered long-distance; whether call duration should have been rounded to the highest minute for billing purposes; how STF should have adjusted its rates in response to rate decreases from FDIC's national long-distance carrier, whether STF was allowed to mark up local exchange carrier charges, and to what extent STF was allowed to escalate equipment charges. The OIG questioned \$996,128 of the total \$3.7 million STF billings based on a strict reading of the contract requirements. Management agreed to disallow the entire amount questioned.

OIG ASSISTS MANAGEMENT IN CONTRACT CLOSEOUTS

Another significant issue that the Corporation continues to face is ensuring the proper and timely closeout of the large volume of expired and expiring RTC contracts that transitioned to FDIC at RTC's sunset on December 31, 1995. Considerable corporate actions are required as contracts expire. All services and goods must be received and accepted, the pertinent documentation obtained, and Corporation-provided equipment and material and all funds belonging to the Corporation must be recovered. In addition, the Corporation must ensure that the contractor provides a complete and final accounting. Finally, the Corporation also faces the challenge of implementing appropriate corrective actions and recovering funds from the contractors for the unallowable or unsupported charges resulting from recommendations made by the OIG.

The OIG's Office of Quality Assurance and Oversight (OQAO), under a Memorandum of Understanding signed prior to RTC sunset, entered into a joint initiative with management to assist with the closeout of contracts that FDIC assumed at RTC sunset. Specifically, the OQAO assumed responsibility for completing reviews of expiring contracts that had been initiated by RTC management. These reviews conducted by OQAO are designed primarily to ensure accountability for all assets assigned under contracts and the accuracy of fees and reimbursable expenses paid to the contractors. Since RTC sunset, FDIC management identified 82 contracts that required an expiration review prior to contract closeout. OQAO

has completed or has in process reviews for each of these contracts.

During this reporting period, OQAO issued 31 reports on expiring contracts which resulted in approximately \$5.7 million in questioned costs. OQAO questioned these costs because they were either unsupported, unauthorized or unallowed. In addition, these reviews identified other financial adjustments, such as income from assets that was due RTC/FDIC and open bank accounts. Since RTC sunset, OQAO has issued a total of 58 reports, including a total of \$8.67 million in questioned costs. A management decision has been issued on 24 of these reports and \$2.15 million in questioned costs; management disallowed \$1.84 million of those questioned costs. Figures 1 and 2 show breakdowns of these questioned amounts.

**Figure 1: Nature of Questioned Costs in RTC Contractor
Expiration Reports (October 1, 1996 - March 31, 1997)**

The OIG's work in the area of contract closeout can also involve our Office of Investigations. For example, OQAO's review of a property management company identified unsupported payments totaling \$93,323 to the contractor's officers, related parties, and third parties. This review also identified disparities in reported rental income and security deposits of \$10,202. Due to the indications of possible irregularities and fraud, OQAO referred these issues to the OIG's Office of Investigations. As a result of the investigation, the president of the company entered into a plea agreement with the U.S. Attorney, District of Massachusetts, admitting to eight counts of embezzlement and one count of taking a kickback. (See Investigations section of this report for additional contractor-related cases.)

**Figure 2: Questioned Costs by Contractor Type
(October 1, 1996 - March 31, 1997)**

In addition, OQAO has assisted FDIC management in resolving a backlog of 1,022 open recommendations that remained at RTC sunset. Of these recommendations, 247 remained unresolved at the beginning of this reporting period. That is, management decisions had not been obtained. OQAO worked with management to reach management decision on all but one of these outstanding recommendations during the

reporting period. Questioned costs associated with these recommendations total \$35.69 million. FDIC management agreed to disallow \$13.09 of the \$35.69 million. Additional information on the resolution of and management actions taken on contractor oversight reviews is contained in Appendix III.

ASSISTANCE AGREEMENT WORK YIELDS RESULTS

During this semiannual reporting period, the Office of Audits completed 18 audits of assistance agreements that FDIC inherited from FSLIC or agreements that FDIC entered into as manager of the FSLIC Resolution Fund. These 18 audits covered various aspects of the assistance agreements, such as net operating loss tax benefits, post closing expenses and receipts, special reserve accounts, book values of transferred assets, and book values of purchased assets. The OIG questioned approximately \$1.1 million as a result of these audits. In one of the audits that covered the quarterly claims filed by and the special reserve account maintained by First Nationwide Bank (FNB), the OIG recommended that the former Division of Resolutions recover \$826,291 in payments to FNB for shared gains. Shared gains are incentive payments made by the FDIC to FNB to minimize losses on the sale of covered assets. As a result of this audit, FNB credited this amount in its final quarterly report and the Division of Resolutions deducted this amount from its subsequent payment to FNB.

The OIG will continue its work in the area of contract and agreement oversight. Ongoing work includes reviews of (1) an FDIC service agreement with a contractor to service certain failed financial institution assets totaling \$1.314 billion, (2) four task orders RTC awarded to a contractor for due diligence services, and (3) five assistance agreement audits. Additionally, the OQAO group will be working to complete the closeout of contracts that FDIC assumed at RTC sunset by the end of 1997.